MARKET REPORT | 1Q/2021

Greater Tucson Multifamily

NORTHMARQ

With Vacancies Tight, Rents Posting Sharp Increases

Highlights

- Vacancies in the Tucson multifamily market remained at historically low levels in the first quarter, supporting rapid rent growth and prompting new development. Investors are responding to the strengthening market conditions by pushing per-unit sales prices higher.
- After vacancy dipped to a 25-year low at the end of last year, the rate held steady at 4.3 percent in the first quarter. Year over year, vacancy in Tucson is down 90 basis points.
- Asking rents continued their upward surge to start 2021, finishing the first quarter at $914 per month. Local rents have spiked 8.9 percent in the past year.
- After a very steady level of activity in 2020, sales velocity dipped approximately 12 percent to start this year. Despite a modest dip in activity, the median price advanced from levels recorded in 2020, and cap rates held steady.

Q1 Snapshot	Tucson Market
Market Fundamentals	
Vacancy	**4.3%**
- Year Over Year Change	**-90 bps**
Asking Rent	**$914**
- Year Over Year Change	**8.9%**
Transaction Activity	
Median Sales Price Per Unit (YTD)	**$85,500**
Cap Rates (Avg YTD)	**5.6%**
Construction Activity	
Units Under Construction	**1,268**
Units Delivered YTD	**386**

Tucson Multifamily Market Overview

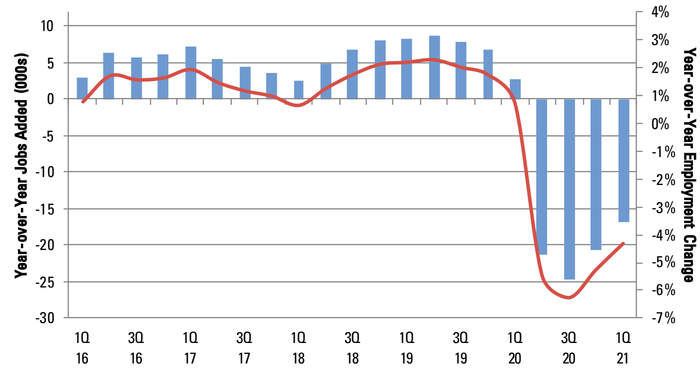
The Tucson multifamily market has been on an extended upswing, a trend that continued during the first quarter. Apartment rents have surged in each of the past three quarters and are increasing at one of the highest rates of any major market in the country. A healthy pace of renter demand has caused vacancies to tighten, despite volatility in the local economy in 2020. With the economic recovery forecast to gain momentum in the coming quarters, multifamily conditions should remain favorable through the remainder of this year.

Investment conditions in Tucson at the beginning of 2021 looked very similar to the market during much of 2020. While most markets recorded a decline in activity during the past year, sales velocity in Tucson gained momentum. In the first quarter, sales were active, although transaction counts did not quite match year-earlier levels. With rents recording robust gains, prices have been on the rise in recent years, and the median price thus far in 2021 is up more than 15 percent from the 2020 figure. Average cap rates have remained in a tight range since the beginning of 2019.

Employment

- Employers in Tucson are slowly adding back workers, following COVID-related losses in the second quarter of last year. During the first quarter, approximately 1,200 jobs were added. Year over year, area employment is down approximately 4.3 percent.
- Financial services are a relatively small portion of Tucson's overall employment, but the sector has been insulated from job losses in the past year. While nearly every other local employment sector has contracted, financial employment has ticked higher by approximately 1.7 percent during the past 12 months.
- E-commerce giant Amazon continues to expand in the Tucson metro. During the first quarter, Amazon broke ground on a new 270,000-square-foot sortation facility near the Tucson airport. When completed, the site will create hundreds of jobs in the local community.
- **Forecast:** Employment growth is expected to pick up as the distribution of the vaccine promotes economic activity. Total employment in Tucson is forecast to expand by approximately 2.6 percent in 2021, gaining 9,500 net jobs.

Employment Overview



Sources: NorthMarq, Bureau of Labor Statistics

Total employment in Tucson is forecast to expand by approximately 2.6 percent in 2021

Vacancy

- Apartment vacancy conditions remained tight in Tucson to start 2021. The rate was 4.3 percent in the first quarter, matching the figure from the fourth quarter of last year. Local vacancy has not been lower than the current rate in nearly 25 years.
- Year over year, vacancy in Tucson declined 90 basis points. After dipping below 5 percent in the second half of last year, the figure has remained essentially flat for the past three quarters.
- Vacancy has been particularly tight in the Oro Valley, Northwest Tucson, and Catalina Foothills submarkets. Vacancy rates in these submarkets were all below 4 percent as of the fourth quarter. Supply growth in these more expensive regions has been minimal since 2017.
- **Forecast:** Apartment construction is forecast to accelerate in 2021, which should put some upward pressure on local vacancy rates. Apartment vacancy in Tucson is forecast to rise 30 basis points this year, ticking up to 4.6 percent.

Vacancy Trends

Sources: NorthMarq, Apartment Insights

Apartment vacancy held steady at 4.3 percent in the first quarter

Rents

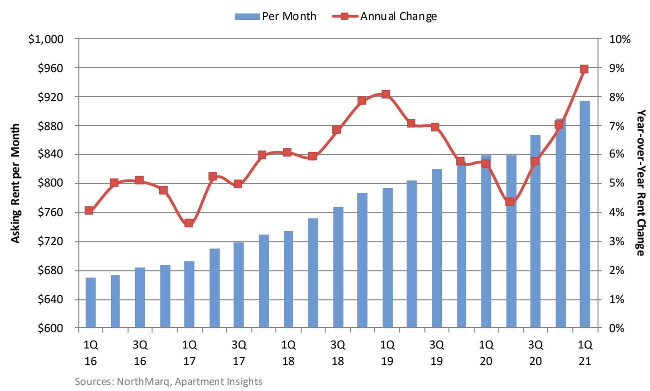
> Local asking rents extended their rapid climb and advanced 2.8 percent in the first quarter of 2021, reaching $914 per month. The increase marked the third straight quarterly gain in excess of 2.5 percent.

> Consistently low vacancy levels are supporting rent growth, particularly with limited competition from new construction. Rents in Tucson are currently recording some of the strongest rent growth in the country, spiking 8.9 percent year over year.

> Rents have been posting strong gains across classes, even in the region's least expensive units. Asking rents in Class C properties have increased 6.6 percent in the past 12 months, reaching $712 per month. Rents in Class B units are on pace to top $1,000 per month in the second quarter.

> **Forecast:** Rent increases are expected for the rest of the year, but the pace will likely level off from the rapid increases recorded in recent quarters. Apartment rents are forecast to reach $945 per month by the end of 2021, an annual increase of 6.3 percent.

Rent Trends



Sources: NorthMarq, Apartment Insights

Tucson is currently posting some of the most robust rental growth in the country

Development and Permitting

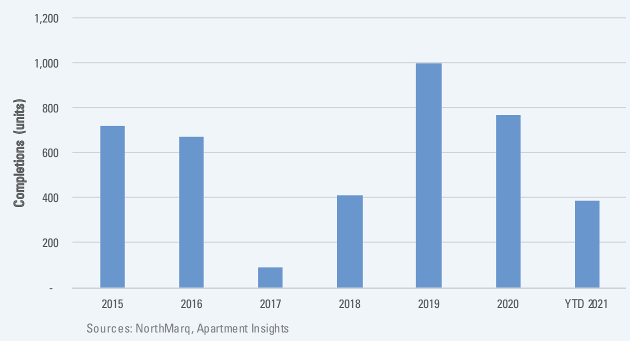
> After slowing in the second half of 2020, multifamily development picked up at the beginning of this year. During the first quarter, developers brought nearly 390 units online.

> Projects totaling approximately 1,270 apartment units are under construction in Tucson, similar to totals from one year ago. New development is concentrated in the University submarket, where three projects totaling nearly 750 units are currently underway.

> During the first quarter of 2021, developers pulled permits for approximately 200 apartment units, closely tracking the figure from the same period a year earlier. Permitting for multifamily housing peaked in 2019 before slowing last year. If vacancies remain low, permitting will likely regain momentum later in the year.

> **Forecast:** Several of the projects that are in development are forecast to be delivered this year. Projects totaling approximately 1,200 units are forecast to deliver in Tucson during 2021, after 765 units were completed in 2020.

Development Trends



Sources: NorthMarq, Apartment Insights

Projects totaling approximately 1,270 apartment units are under construction in Tucson

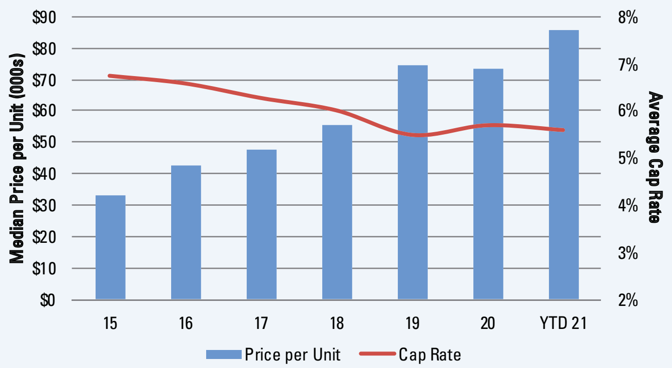
Multifamily Sales

> Total transaction activity in the first quarter of 2021 lagged levels from the same period one year earlier by approximately 12 percent. The bulk of the activity that occurred during the first quarter included private capital sales ranging from $3 million to $6 million, and larger transactions in the $20-million to $35-million range.

> Strong property fundamentals supported price increases to start the year. In deals that closed during the first quarter, the median sales price was $85,500 per unit, a 16 percent increase from the median price in 2020.

> Cap rates averaged approximately 5.6 percent during the first quarter, closely tracking 2020 levels. Some properties have traded with cap rates near 4.5 percent.

Investment Trends



Sources: NorthMarq, CoStar

In deals closed during the first quarter, the median sales price was $85,500 per unit

Recent Transactions in the Market

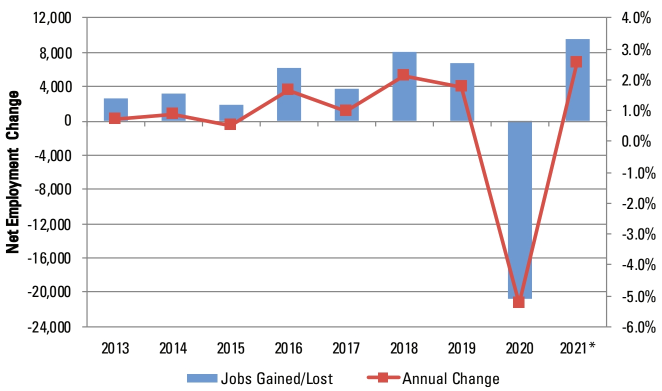
MULTIFAMILY SALES ACTIVITY				
Property Name	**Street Address**	**Units**	**Sales Price**	**Price/Unit**
Tierra Vida Luxury Apartment Homes	1970 W Old Magee Trl, Tucson	200	$35,750,000	$178,750
Catalina Ridge	7400 E Golf Links Rd., Tucson	428	$34,750,000	$97,339
Agave at Twenty Two	8485 E 22nd St., Tucson	266	$33,450,000	$125,752
La Mirada	4415 E Grant Rd., Tucson	201	$18,000,000	$89,552

Looking Ahead

The momentum in the Tucson multifamily market carried over from 2020 to the first quarter of this year, setting the stage for another year of robust performance. The market's consistently low vacancy rate continues to spark rent growth and fuel new development. The delivery of new apartment units is on pace to hit an eight-year high in 2021, which will likely result in a modest uptick in vacancy, despite renter demand levels that are forecast to outpace 2020 levels. More than half of the units that are under construction are located in the University submarket. Demand in the University submarket will likely receive a boost in the third quarter as the University of Arizona fully resumes in-person classes.

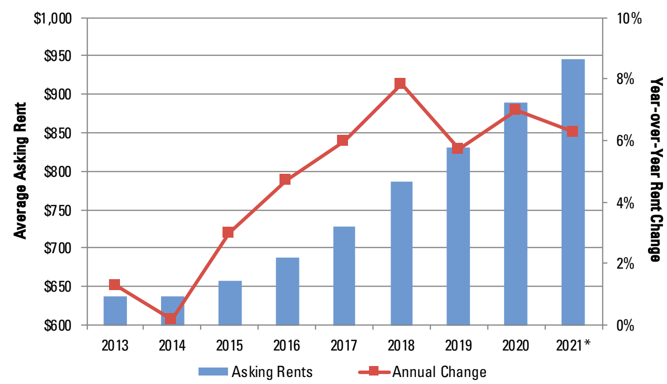
While area property fundamentals are forecast to remain healthy in 2021, investment activity in Tucson may level off a bit. Transaction counts in the first quarter trailed levels from one year earlier, and Tucson was one of the few markets that did not record sales velocity declines in 2020. Fewer properties may change hands in the year ahead, particularly if interest rates trend higher as the economy gains momentum. To this point in 2021, cap rates have held steady, following several years of compression. Any significant increases in borrowing costs could widen the buyers' and sellers' expectations gap in the coming quarters.

Employment Forecast



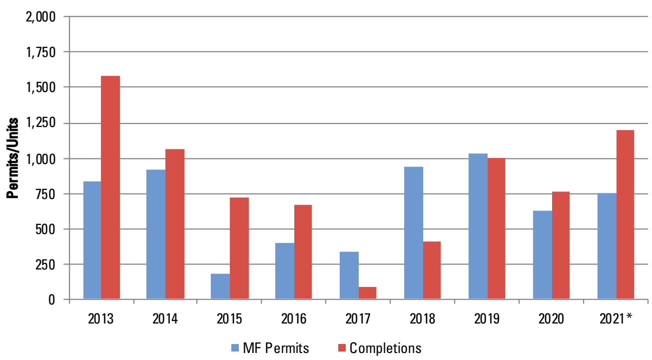
* Year End Forecast
Sources: NorthMarq, Bureau of Labor Statistics

Rent Forecast



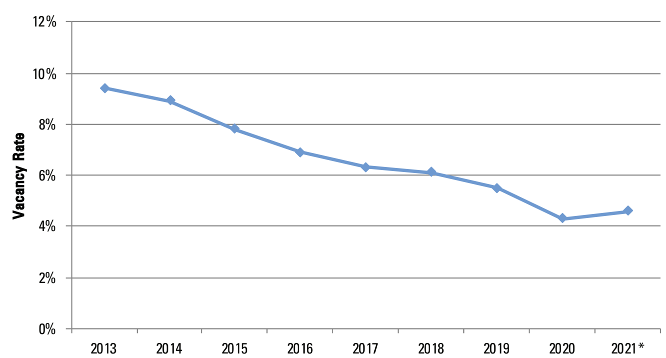
* Year End Forecast
Sources: NorthMarq, Apartment Insights

Construction & Permitting Forecast



* Year End Forecast
Sources: NorthMarq, Apartment Insights, Census Bureau

Vacancy Forecast



* Year End Forecast
Sources: NorthMarq, Apartment Insights

About NorthMarq

As a capital markets leader, NorthMarq offers commercial real estate investors access to experts in debt, equity, investment sales, and loan servicing to protect and add value to their assets. For capital sources, we offer partnership and financial acumen that support long- and short-term investment goals. Our culture of integrity and innovation is evident in our 60-year history, annual transaction volume of more than $14 billion, loan servicing portfolio of more than $61 billion and the multi-year tenure of our nearly 600 people.

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